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IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

ATLANTIC RICHFIELD COMPANY; ARCO PIPELINE COMPANY; EXXON CORPORATION; EXXON PIPELINE COMPANY; BP ALASKA INC.; SOHIO ALASKA PETROLEUM COMPANY; and SOHIO PIPE LINE COMPANY,
Appellants,

v.

STATE OF ALASKA, *et al.*,
Appellees.

On Appeal from the Supreme Court of Alaska

MOTION TO DISMISS OR AFFIRM

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TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES iii

INTRODUCTION 1

STATEMENT OF THE CASE 5

THE QUESTIONS PRESENTED ARE INSUBSTANTIAL 10

I. THE CENTRAL QUESTION PRESENTED—WHETHER SEPARATE ACCOUNTING MAY CONSTITUTIONALLY CO-EXIST WITH FORMULA APPORTIONMENT—WAS ANSWERED BY THIS COURT IN THE AFFIRMATIVE IN *CONTAINER CORP.* 10

A. Taxpayers' Arguments Are Based On A Conceptual Trick 11

1. It Is Perfectly Proper For Alaska To Levy A Tax On 100% Of Income Earned In The State 11

2. No Other State Is Entitled To "Tax A Share" Of Oil Production Income Earned In Alaska 13

B. The *Container Corp.* Decision Controls This Case 14

C. Taxpayers Misrepresent This Court's Decision In *Exxon v. Wisconsin* And Misapply Cases Dealing With Gross Receipts And Property Taxes 15

II. THIS COURT SHOULD DISMISS TAXPAYERS' APPEAL BECAUSE THEY DID NOT EVEN ATTEMPT TO SHOW THAT AS 43.21 DISPROPORTIONATELY ATTRIBUTES INCOME TO THE STATE 18

TABLE OF CONTENTS—Continued

Page

A. Taxpayers Have Presented No Evidence Showing That Alaska's Separate Accounting Method Disproportionately Attributes Income To The State 19

B. AS 43.21 Properly Accounts For Out-of-State Contributing Activities 21

III. NONE OF TAXPAYERS' OTHER POINTS IS SUBSTANTIAL 23

A. Alaska's Corporate Income Tax Statute Is Internally Consistent 23

B. Alaska's Division-of-Income Method Does Not Discriminate Against Interstate Commerce 24

C. The Measure Of Alaska's Income Tax Is Reasonably Related To Taxpayers' Alaskan Activities 26

IV. PRUDENTIAL CONSIDERATIONS OFFER ADDITIONAL REASONS FOR NOT GIVING PLENARY REVIEW TO THIS APPEAL 28

CONCLUSION 30

APPENDIX 1a

TABLE OF AUTHORITIES

Cases Page

Armco, Inc. v. Hardesty, 104 S. Ct. 2620 (1984) 25
Bass, Ratcliff & Gretton, Ltd. v. State Tax Commission, 266 U.S. 271 (1924) 20
Boston Stock Exchange v. State Tax Commission, 429 U.S. 318 (1977) 25
Butler Brothers v. McColgan, 315 U.S. 501 (1942) 20
Commonwealth Edison Co. v. Montana, 453 U.S. 609 (1981) 26
Container Corp. of America v. Franchise Tax Board, 463 U.S. 159 (1983) ..... *passim*
Evco v. Jones, 409 U.S. 91 (1972) 16
Exxon Corp. v. Wisconsin Department of Revenue, 447 U.S. 207 (1980) 15, 16
Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell, 283 U.S. 123 (1931) 18, 20
J.D. Adams Manufacturing Co. v. Storen, 304 U.S. 307 (1938) 16
Japan Line v. County of Los Angeles, 441 U.S. 434 (1979) 16, 17
Magnolia Petroleum Co. v. Oklahoma Tax Commission, 190 Okla. 172, 121 P.2d 1008 (1941) ..3, 22, 28
Metropolitan Life Insurance Co. v. Ward, 105 S. Ct. 1676 (1985) 24
Mobil Oil Corp. v. Commissioner of Taxes, 445 U.S. 425 (1980) 16, 29
Moorman Manufacturing Co. v. Bair, 254 N.W.2d 737 (Iowa 1977), *aff'd*, 437 U.S. 267 (1978) 21
Moorman Manufacturing Co. v. Bair, 437 U.S. 267 (1978) ..... *passim*
Norfolk & Western Railway v. Missouri State Tax Commission, 390 U.S. 317 (1968) 18, 20, 29
Norfolk & Western Railway v. North Carolina ex rel. Maxwell, 297 U.S. 682 (1936) 20
Standard Oil Co. v. Peck, 342 U.S. 382 (1952) 16
Texas Co. v. Cooper, 236 La. 380, 107 So. 2d 676 (1958) 3, 12, 19, 28
Underwood Typewriter Co. v. Chamberlain, 254 U.S. 113 (1920) 12, 18, 20, 22

TABLE OF AUTHORITIES—Continued

	Page
Webb Resources, Inc. v. McCoy, 194 Kan. 758, 401 P.2d 879 (1965)	3, 19, 28
Westinghouse Electric Corp. v. Tully, 104 S. Ct. 1856 (1984)	25
Wisconsin v. J.C. Penney Co., 311 U.S. 435 (1940)	18, 29
United States Statutes	
26 U.S.C. §§ 861-64	2, 7
§ 907(d)	2
United States Regulations	
Treas. Reg. § 1.482-2(b)(1)	22
§ 1.482-2(b)(3)	22
§ 1.482-2(b)(6)	2
§ 1.482-2(b)(7)	22
§ 1.482-2(e)(1)(ii)	2
§ 1.861-8(a)(1)	2, 8
§ 1.861-8(b)(3)	8
§ 1.861-8(c)(1)	8
§ 1.863-1(b)(1)	2, 7
§ 1.863-1(c)	2, 8
State Statutes and Regulations	
Alaska Stat. § 37.13.010(a)	28
§§ 43.21.010-.120	1
§ 43.21.020	2
§ 43.21.020(b)	2, 7
§ 43.21.020(c)	8
§ 43.21.020(c)(9)	8
§ 43.21.040	7-8
15 Alaska Admin. Code § 21.130(b)	7
§ 21.290(b)	23
La. Admin. Code art. 47:244.3.A (1975)	8, 22
47:244.3.B.1.b	7
47:244.3.B.3	8, 22
Miss. Code Ann. § 27-7-23(c)(2)(B) (7 Supp. 1985)	8, 22
§ 27-7-23(c)(2)(B)(iii)	7

TABLE OF AUTHORITIES—Continued

Page

Miss. Admin. Reg. 1.27-7-23(7)(c)(2) (1979) 8, 22

Okla. Stat. Ann. tit. 68, § 2358, A.4.a (West. Supp. 1984) 7, 8, 22

Examples of State Statutes and Regulations Embodying Division-of-Income Rules Different From UDITPA Formula Apportionment ..... Appendix

Legislative Materials

S. 1113, 99th Cong., 1st Sess. (1985) 30

Treatises and Periodicals

Department of Education, *Alaska Blue Book* (1985) 10

J. Hellerstein, *State Taxation: Corporate Income and Franchise Taxes* (1983) 2, 5, 6

OECD Model Convention for the Avoidance of Double Taxation with Respect to Taxes on Income and Capital, *reprinted in* 1 Tax Treaties (CCH) ¶ 151 2

P. Hartman, *Federal Limitations on State and Local Taxation* (1981) 17

Pierce, *The Uniform Division of Income for State Tax Purposes*, 35 Taxes 747 (1957) 5

Rudolph, *State Taxation of Interstate Business: The Unitary Business Concept and Affiliated Corporate Groups*, 25 Tax L. Rev. 171 (1970) 2

Statistical Abstract of the United States (103d ed. 1982-83) 2

U.S. Energy Information Administration, *Monthly Energy Review* (Sept. 1983) 9

U.S. General Accounting Office, *Key Issues Affecting State Taxation of Multi-Jurisdictional Corporate Income Need Resolving* (1982) 3

U.S. General Accounting Office, *Response to Questions About the Windfall Profit Tax on Alaskan North Slope Crude Oil* (1984) 7

U.S. Treasury Department, Draft Model Income Tax Treaty, June 16, 1981, *reprinted in* 1 Tax Treaties (CCH) ¶ 158 2

TABLE OF AUTHORITIES—Continued

Miscellaneous Page

Statement by the President, State Taxation of Multinational Corps., 21 Weekly Comp. Pres. Doc. 1368 (Nov. 8, 1985) 29

Uniform Division of Income for Tax Purposes Act § 18 (1978) 5

MOTION TO DISMISS OR AFFIRM

The State of Alaska respectfully moves this Court to dismiss this appeal on the ground that the appeal does not present a substantial federal question, or, in the alternative, to summarily affirm the judgment below.

INTRODUCTION

The State of Alaska imposes on every corporation a 9.4% tax on net income derived from sources within the State. This tax applies uniformly to multistate corporations and to those doing business only in Alaska, but it is levied only on the portion of a multistate corporation's income earned within the State.

For most industries, Alaska uses the standard three-factor apportionment formula to estimate the income earned in the State by a multistate taxpayer. In 1978, when oil production became Alaska's predominant economic activity, the Alaska Legislature determined that continued use of a formula unsuited to oil production would attribute to Alaska only about one-quarter of the oil production income actually earned in the State. The Legislature found that as a result, oil producers would pay an effective tax rate on Alaskan income of only 2 to 3%, far below the statutory 9.4% uniform rate. To equalize effective tax rates for all corporate taxpayers, the Legislature enacted the Oil and Gas Corporate Income Tax, Alaska Stat. §§ 43.21.010-.120 (1978) [hereinafter "AS 43.21"]. Instead of a formula, AS 43.21 used the division-of-income method widely recognized to be the most accurate for oil production income: arm's length geographical separate accounting.[1]

In an attempt to mislead this Court into believing a substantial issue is presented here, appellants [herein-

[1] See pp. 7-8 *infra*. AS 43.21 also applies separate accounting to determine the income generated by natural gas production and by pipeline transportation of oil or gas within the State. For simplicity, however, we refer only to "oil production income."

after "taxpayers"] portray Alaska's adoption of traditional separate accounting as an aberrational overreaching of the State's legitimate taxing authority. This position is wholly disingenuous. The majority of major oil-producing States require use of separate accounting to divide the oil production income of multistate companies,[2] as does the Internal Revenue Code for determining the U.S. oil production income of multinational corporations that produce oil in this country for sale abroad.[3] Tax conventions and treaties to which the United States is a party also require separate accounting.[4] Alaska's separate accounting statute is *identical* to these other separate accounting laws in all material respects.

The leading experts in state taxation acknowledge that separate accounting, not formula apportionment, is "the prevailing method . . . for reporting income from oil production." [5] In the most comprehensive federal study of state taxation in several decades, the Comptroller General of the United States explained that oil-producing States generally require separate accounting for oil production

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[2] Of the five largest oil producing States, three (Oklahoma, Louisiana, and Alaska) require separate accounting. *See* Appendix to Jurisdictional Statement 17a n.25 [hereinafter "App."] and notes 13 & 16, *infra*. Texas does not have a corporate income tax. Only California requires formula apportionment. *See Statistical Abstract of the United States* 730 (103d ed. 1982-83).

[3] 26 U.S.C. §§ 861-64; Treas. Reg. §§ 1.861-8(a)(1), 1.863-1(b)(1), -1(c); Treas. Reg. §§ 1.482-2(b)(1), (3), (6), and -2(e)(1)(ii). The foreign tax credit provisions of the Code also employ separate accounting for oil and gas production. *Compare* 26 U.S.C. § 907(d) *with* AS 43.21.020.

[4] OECD Model Convention for the Avoidance of Double Taxation with Respect to Taxes on Income and Capital, *reprinted in* 1 Tax Treaties (CCH) ¶ 151; U.S. Treasury Dep't Draft Model Income Tax Treaty, June 16, 1981, *reprinted in* 1 Tax Treaties (CCH) ¶ 158.

[5] Rudolph, *State Taxation of Interstate Business: The Unitary Business Concept and Affiliated Corporate Groups*, 25 Tax L. Rev. 171, 191 (1970); *see* J. Hellerstein, *State Taxation: Corporate Income and Franchise Taxes* 396 n.309 (1983), *quoted infra* p. 6.

income because it "conforms more to [oil production companies'] financial accounting practices and, for these specific situations, *more accurately reflects income than* formula apportionment." [6]

There is also unanimity among the courts. Every court that has considered the constitutionality of separate accounting for oil production income has not only upheld its use, but has found that it is a *more* accurate method of attributing oil production income than formula apportionment.[7]

The central issue actually presented by this appeal is whether the Constitution prohibits Alaska from using traditional arm's-length separate accounting, and instead requires formula apportionment. That issue was foreclosed by this Court's decision just two years ago in *Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159 (1983). To avoid the clear controlling force of that precedent, taxpayers distort the facts and mischaracterize this Court's recent key decisions on state taxation. Their arguments reduce to two simple—but clearly erroneous—propositions, neither of which merits plenary review.

Taxpayers' first claim is that AS 43.21 is an "unapportioned" tax which taxes "100% of something that other states are entitled to tax by apportionment." Jurisdictional Statement at 9, 12 [hereinafter "J.S."]. This argument is based on a conceptual trick: the false notion that other States' formula apportionment laws entitle them to reach into Alaska and tax a share of the same income Alaska taxes. This Court has already seen through and soundly rejected an identical mischaracteri-

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[6] U.S. General Accounting Office, *Key Issues Affecting State Taxation Of Multi-Jurisdictional Corporate Income Need Resolving* 3 (1982) (emphasis added) [hereinafter "GAO Report: Key Issues"].

[7] *Webb Resources v. McCoy*, 194 Kan. 758, 401 P.2d 879, 889 (1965); *Texas Co. v. Cooper*, 236 La. 380, 107 So.2d 676, 690 (1958); *Magnolia Petroleum v. Oklahoma Tax Comm'n*, 190 Okla. 172, 121 P.2d 1008, 1011-13 (1941).

zation of the purpose and operation of separate accounting and formula apportionment in *Container Corp.*

Second, based solely upon this conceptual error, taxpayers argue that use of separate accounting and formula apportionment by different States inevitably causes multiple taxation; and that since most States use formula apportionment, the Commerce Clause should now be interpreted to forbid other States' use of separate accounting. This misguided argument was squarely rejected in *Container Corp.* This Court's holding there that the concurrent use of separate accounting and formula apportionment is perfectly acceptable, 463 U.S. at 188, 195, is fully controlling here.

Container Corp. reaffirmed this Court's long tolerance of different methods of income allocation, as long as such methods do not result in a grossly disproportionate attribution of a multistate taxpayer's income to the taxing State. As the Court there said, "we have long held that the Constitution imposes no single formula on the States." 463 U.S. at 164. For that reason, the Court has consistently imposed upon a taxpayer "the 'distinct burden,' " *id.* at 164 (citations omitted), of proving "*by 'clear and cogent evidence'* that the income attributed to the [taxing] State is in fact 'out of all appropriate proportions to the business transacted . . . in that State,' or has 'led to a grossly distorted result.' " *Id.* at 170 (emphasis added) (quoting, *inter alia*, *Moorman Manufacturing Co. v. Bair*, 437 U.S. 267, 274 (1978)).

Taxpayers in this case made a deliberate, strategic judgment below not even to try to adduce such evidence. Instead, taxpayers litigated this case as a *per se* attack on separate accounting. But as the court below recognized, *Container Corp.* has flatly foreclosed that approach. Taxpayers offer no reason why just two years later this Court should reconsider *Container Corp.*, abandon its longstanding deference to the States in the field of taxation, or invalidate a division-of-income method favored by the United States, by international

treaty and practice, and by the majority of major oil-producing States.

STATEMENT OF THE CASE

At Statehood in 1959, Alaska became the first State to adopt the Uniform Division of Income for Tax Purposes Act [hereinafter "UDITPA"], now used by many States. In general, UDITPA (and the Multistate Tax Compact, which incorporates UDITPA) estimates the in-state income of a multistate company by use of a mathematical formula incorporating certain indicators of business activity within the State. The formula averages the fractions (or percentages) of the taxpayer's nationwide property, sales, and payroll that are found within the taxing State, and then multiplies the resulting average percentage by the taxpayer's nationwide income.[8]

UDITPA's formula assumes that for most mercantile and manufacturing industries, income is generated in equal proportions by these three "factors" or sources of profit, and therefore uses them to approximate roughly the income earned in the taxing State. It has long been recognized, however, that the "three-factor" formula is the product of political compromise,[9] and that for some industries it does not produce a fair estimate of in-state income.[10] UDITPA therefore permits a State to require "in respect to all or any part of the taxpayer's business activity" reasonable alternative methods of income allocation—including separate accounting. UDITPA § 18. Most States have, in fact, enacted exceptions to the three-factor formula for various industries, including natural

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[8] Thus, for example, if 2% of a company's nationwide property, 3% of its nationwide sales, and 7% of its nationwide payroll are located in Wisconsin, then under UDITPA's formula, Wisconsin would be entitled to assume that 4% of the company's nationwide income was earned in Wisconsin, and levy a tax on that amount.

[9] *See* Pierce, *The Uniform Division of Income for State Tax Purposes*, 35 Taxes 747, 750 (1957).

[10] J. Hellerstein, *State Taxation*, *supra* n.5, at 689; *see* App. 16a.

resource extraction, financial oragnizations, utilities, construction, and transportation.[11]

Most major oil-producing States have chosen separate accounting for oil production income because the UDITPA formula grossly *underattributes* the in-state income of a producing company. As the leading academic commentator in the field of state taxation has observed, "[t]he three-factor formula may be inappropriate to such industries as petroleum . . . in failing to give adequate weight to the State of origin of the natural resource on which the industry is based, and which is basic to the profit of the enterprise." J. Hellerstein, *State Taxation*, *supra* n.5, at 396 n.309.

This underattribution is the result of the fact that none of the three UDITPA factors measures the major source of oil production profits, the value of the crude oil itself. The property factor grossly undervalues an oil-producing company's in-state assets because, under oil industry accounting practices only lease acquisition costs —and not the value of the oil reserves themselves—are carried on the taxpayers' books as "property". Thus there is no dispute, as the court below found, that "the Prudhoe Bay field is valued [in the UDITPA property factor] at about *one percent* of its actual worth." App. 17a (emphasis added). The payroll factor also underrepresents oil production activities, because oil production is not labor-intensive. And the sales factor severely underattributes income to an oil-producing State like Alaska, which has little market for the resource it produces.

When oil began to dominate the Alaskan economy it was imperative that Alaskan oil production income be determined accurately. The Alaska Legislature responded to the formula's defects by enacting an exception to UDITPA, AS 43.21, that required use of separate accounting to calculate the portion of a company's oil pro-

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[11] *See* Appendix for a partial listing of more than sixty such industry-specific allocation rules.

duction income earned in the State. Under separate accounting, a taxpayer's gross income from oil production is the value of the oil produced in the State, before it leaves the State's borders. In other words, under AS 43.21, Alaskan *gross* oil production income equals the number of barrels of crude oil produced in the State multiplied by the wellhead value of each barrel, *i.e.*, the crude oil's market value at the point of production.[12] This concept of gross oil production income is the same as that used by other oil-producing States that require separate accounting,[13] and in various provisions of the Internal Revenue Code and U.S. Treasury Regulations.[14] Contrary to taxpayers' misleading innuendos, by using the in-state market value of the crude oil, *separate accounting completely excludes from taxation all profits earned by taxpayers from all activities occurring "downstream" from the wellhead*, *i.e.*, transportation profits, profits from refining the crude oil, and profits from distributing and marketing retail products.[15]

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[12] AS 43.21.020(b). When the oil is sold in Alaska, that sale price is used to determine wellhead value. When there is no such sale—for example, when taxpayers transfer the crude oil from their production departments to their own refining departments, and "deem" the transfer to have taken place outside Alaska—the in-state market value of the oil must be derived. This is done by taking the closest available out-of-state market price, and deducting all costs of transporting the crude oil from the wellhead to that point (including the transporter's profit). 15 Alaska Admin. Code § 21.130(b) [hereinafter "AAC"]. This "net-back" approach has traditionally been used throughout the oil industry for purposes such as calculating windfall profit taxes, royalty payments, and severance taxes. *See, e.g.*, U.S. General Accounting Office, *Response to Questions About the Windfall Profit Tax on Alaskan North Slope Crude Oil*, 1 & appendix 10 (1984).

[13] La. Admin. Code art. 47:244.3.B.1.b (1975); Miss. Code Ann. § 27-7-23(c)(2)(B)(iii) (7 Supp. 1985); Okla. Stat. Ann. tit. 68, § 2358, A.4.a. (West Supp. 1984).

[14] 26 U.S.C. §§ 861-64; Treas. Reg. § 1.863-1(b)(1).

[15] Under AS 43.21.040, the in-state *refining* and *marketing* income of oil companies is separated out from production income and deter-

To arrive at net (taxable) income, separate accounting deducts from gross income *all* of the direct and indirect costs of producing Alaskan oil, whether they are incurred in or out of the State. Deductible costs include all direct operating costs, all taxes (including federal windfall profit taxes, severance taxes, conservation and property taxes), royalties, current amortization, unsuccessful exploration costs, lease acquisition costs, and capitalized interest. AS 43.21.020(c). General corporate overhead and administrative expenses attributable to the production of Alaskan oil are also deducted. AS 43.21.020 (c)(9). The expenses and deductions permitted by Alaska's separate accounting statute are substantially identical to those permitted by the separate accounting laws of other oil-producing States, and by the Internal Revenue Code.[16]

Alaska's separate accounting law was in effect from 1978 through 1981. During that period, these taxpayers earned over $21 billion in profits from the production of oil in Alaska, and paid approximately $2 billion in corporate income taxes to the State. In light of taxpayers' contention that Alaska has singled them out for "burdensome" taxation, it is important to recognize that these taxpayers paid a large amount of taxes for no other reason than that, because of an unanticipated *four-fold in-*

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mined by an apportionment formula that *excludes* all oil production income, and all the payroll, property and sales associated with oil production. Since these taxpayers have no refineries in Alaska, and sell virtually no refined products there, Alaska taxes only a negligible fraction of taxpayers' worldwide refining and marketing income, corresponding to the refining and marketing factors found in the State. *See* pp. 23-24 *infra*.

[16] La. Admin. Code art. 47:244.3.A, B.3 (1975); Miss. Code Ann. § 27-7-23(c)(2)(B) (7 Supp. 1985); Okla. Stat. Ann. tit. 68, § 2358, A.4.a (West Supp. 1984); Miss. Admin. Reg. 1.27-7-23(7)(c)(2) (1979); Treas. Reg. §§ 1.863-1(c), 1.861-8(a)(1), -8(b)(3) and -8(c)(1).

crease in world crude oil prices,[17] they realized a phenomenal increase in oil production profits in the late 1970's and early '80's.

Although the State was not required to do so, it introduced in the court below substantial evidence showing that the income *taxpayers themselves* attributed to Alaskan oil production—in their own annual reports, in reports to federal agencies (including the SEC and the Department of Energy), and in income tax returns filed with other States—was equal to or greater than their Alaskan income as determined by AS 43.21. R. 16912-17. That evidence confirmed that the Alaska Legislature was right on the mark in finding that separate accounting is a far more accurate division-of-income system for oil production than formula apportionment.

It is also essential to realize that taxpayers paid, and would pay under any division-of-income method, a very high percentage of all Alaskan corporate income taxes simply because their profits dwarf all other corporate earnings in Alaska. Alaska is not blessed with a diverse economy. Prior to the first production of oil from Prudhoe Bay in 1977, Alaska's economy was that of a struggling frontier. When oil production began, it virtually eclipsed all other economic activity in the State.[18] Thus,

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[17] In 1976, before Prudhoe Bay production began, American crude oil had an average wellhead value of $8.19 a barrel. In 1978, when AS 43.21 was enacted, oil was at $9.00 a barrel. By 1981, domestic crude had risen to $31.77 a barrel, with no commensurate increase in the *cost* of producing this oil. *See* U.S. Energy Information Administration, *Monthly Energy Review* 86 (Sept. 1983).

When the *increase* in crude oil prices over the four tax years is multiplied by the prevailing rate of North Slope production—approximately 1.6 million barrels per day—the *additional profit bonanza* realized by *all* North Slope producers *attributable to skyrocketing oil prices alone* was over $24 billion.

[18] An "essentially complete" description of the manufacturing sector in the State is: two pulp mills, three small refineries, two natural gas plants, and several seafood processing plants. R. 16970. Alaska's only significant corporate tax base is the harvesting of natural

even if taxpayers' Alaskan income had been estimated by the three-factor formula, these three taxpayers would *still* have paid approximately 83% of *all* the income taxes collected by the State.[19]

In this litigation, despite an ample opportunity to do so, taxpayers never submitted evidence of any kind from which the trial court could reasonably have found that AS 43.21 attributed income to Alaska that was in any way different from what taxpayers actually earned there —much less "out of all appropriate proportion" to it. Taxpayers were thus left with an entirely theoretical challenge to separate accounting, a challenge now completely foreclosed by the recent *Container Corp.* decision. Recognizing this, the Alaska Supreme Court affirmed the trial court's order granting summary judgment to the State.

THE QUESTIONS PRESENTED ARE INSUBSTANTIAL

I. THE CENTRAL QUESTION PRESENTED—WHETHER SEPARATE ACCOUNTING MAY CONSTITUTIONALLY CO-EXIST WITH FORMULA APPORTIONMENT—WAS ANSWERED BY THIS COURT IN THE AFFIRMATIVE IN *CONTAINER CORP.*

The cornerstone of taxpayers' appeal is their assertion that the use of separate accounting (or the "arm's-length

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resources. *Id.* The impact of oil production activity on Alaska's otherwise marginal economy can be appreciated by comparing it with the State's next most valuable resource, seafood. In 1981, the gross value of fish harvested in Alaska waters was approximately *one-twentieth* of the wellhead value of oil produced in that year. Dep't of Education, *Alaska Blue Book* 275 (1985).

[19] Taxpayers claim that under AS 43.21 the oil industry paid 95% of the income taxes in Alaska, J.S. at 3, and under UDITPA they would have paid about one-quarter of that amount, App. 181a. If, out of $100 of total State income tax revenue, oil companies paid $95 under AS 43.21, they would pay only $23.75 (one-quarter) under UDITPA. That would be 83% of the sum of $23.75 and $5 (non-oil income tax revenue).

method") by one State combined with the use of formula apportionment by other States inevitably leads to multiple taxation. But that precise contention was expressly rejected by this Court in *Container Corp.*:

> Here . . . we are faced with two distinct methods of allocating the income of a multinational enterprise. The "arm's-length" approach divides the pie on the basis of formal accounting principles. The formula apportionment method divides the same pie on the basis of a mathematical generalization. Whether the combination of the two methods results in the same income being taxed twice or in some portion of income not being taxed at all is dependent solely on the facts of the individual case.

463 U.S. at 188 (footnote omitted). This holding—that the two methods are not inherently incompatible, and, in the Court's words, do not "create an automatic 'asymmetry' "—controls this case. *Id.* at 194-95.

Ignoring *Container Corp.*, taxpayers repeatedly assert that "a state may not attribute to itself for taxation 100% of something other states are entitled to tax by apportionment," J.S. at 9-10 (footnote omitted); *see* J.S. at 12, 13, 13-14, and that, in using formulas, other States tax "a share" of that "something". J.S. at 11, 12; *see* J.S. at 13, 13-14.

This argument is nothing but a conceptual trick. Quite simply, neither apportionment formulas nor separate accounting are intended to—or do in fact—operate the way taxpayers contend.

A. Taxpayers' Arguments Are Based On A Conceptual Trick.

1. *It Is Perfectly Proper For Alaska To Levy A Tax On 100% Of Income Earned In The State.*

There is absolutely nothing wrong with Alaska applying its 9.4% tax rate to 100% of the income that its division-of-income rule reasonably attributes to the State. Every State, no matter what method it uses to divide

income, levies a tax on *all* of the income it estimates was generated within its borders. Thus, taxpayers' litany that "Alaska taxes 100%" is true only in the same sense that California, Oklahoma, and Wisconsin also tax "100%" of California-, Oklahoma-, and Wisconsin-generated income, respectively. Each taxes 100% of the *portion* of a taxpayer's multistate net income that the State's division-of-income rules attribute to that State.

Taxpayers also mischaracterize the nature of the portion that Alaska taxes. AS 43.21 does *not*, as taxpayers allege, tax "all the net income that results when crude oil from Alaskan wells is sold in the Lower 48 States." J.S. at 7. Rather, it defines oil production gross income as the market value of the crude oil at the wellhead. It thereby excludes *all* income derived from the subsequent transportation, refining, distribution, marketing and final sales of Alaskan crude oil and its products. All production costs are then deducted. The remainder is clearly *not* all of the income taxpayers ultimately derive from Alaskan oil. As demonstrated in the oil barrel chart set out in the opinion below, App. 5a n.6, the total revenue taxpayers derived from the sale of a barrel of Alaskan crude oil was $26.64. Alaska levied its tax on only $6.77 of this amount, the net profits derived solely from the production of oil in Alaska.[20]

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[20] Taxpayers would like this Court to believe that AS 43.21 is flawed because most of the oil produced in Alaska is not "sold" in the State. It is not clear, however, what this purported flaw is. First, most Alaskan crude is not *sold* at all—it is transferred to the taxpayers' self-owned refineries in the lower 48 States. R. 12692, App. 296a. Second, AS 43.21 is not a forbidden unapportioned gross receipts tax levied by the origin state "on" interstate sales. It is a *net* income tax that sometimes must use an out-of-state value (refinery gate price) in deriving the market price of crude oil before it leaves the State. *See Texas Co. v. Cooper*, 107 So. 2d at 687. A *net* income tax *may* use an origin-state sales factor (*Moorman*, 437 U.S. at 278 n.13), or may ignore the contribution of sales to income entirely. *Underwood Typewriter v. Chamberlain*, 254 U.S. 113, 118 (1920).

2. *No Other State Is Entitled To "Tax A Share" Of Oil Production Income Earned In Alaska.*

Contrary to taxpayers' misleading contention, States that use formulas do not—and may not—tax a share of the income generated by taxpayers' activities in Alaska. An apportionment formula is not a license to engage in extraterritorial taxation. Rather, it is a method that a State constitutionally may use to estimate (albeit roughly) the income earned by activities *within* the State.

The common three-factor formula estimates a State's tax base by assuming that a State's percentage of a business's total net income is roughly equal to the average of the fractions of its total payroll, property, and sales that are located in the State. *Container Corp.*, 463 U.S. at 170, 183. The sole purpose of the formula, however, is to arrive at "a rough approximation of a corporation's income . . . *within the taxing State*," *Moorman*, 437 U.S. at 273 (emphasis added), not to tax a share of the income it earns in every other State.[21]

Taxpayers claim to have proved "actual" double taxation in this case because, in their words, "42 other states actually tax a share of Exxon's production income from Alaskan oil: those states treat a total of 30% of that income as 'their' income, in addition to the 100% that Alaska says is 'its' income," J.S. at 11 n.10 and 11-12. This 30% figure is nothing more than

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[21] If Wisconsin averages the fractions of Exxon's property, sales and payroll found in Wisconsin and arrives at an apportionment fraction of 2%, which it then multiplies by Exxon's income earned in all fifty States, Wisconsin is still only estimating and taxing—indeed, is constitutionally *bound* only to tax—income earned in Wisconsin. It is *not* taxing 2% of Exxon's income earned in Alaska, as appellants claim, any more than it is taxing 2% of Exxon's income earned in California (which also uses a formula), in Texas (which has no income tax), or in Oklahoma (which, like Alaska, separately accounts). Rather, if 2% of Exxon's factors are in Wisconsin, then Wisconsin may constitutionally assume for tax purposes that income follows those factors in rough proportion, and may therefore levy a tax on 2% of Exxon's nationwide income.

the sum of the apportionment percentages calculated by the 42 States that use formula apportionment. App. 407a. In other words, the 42 formula States attribute to themselves (and thus tax) 30% of Exxon's nationwide production, refining and retailing income. Alaska, of course, does not tax 100% of Exxon's nationwide income; rather, it levies its tax on 100% of the *portion* of Exxon's *production income* that it determines was *earned in Alaska*. It is thus a trick and a deception to claim the 130% "double taxation" taxpayers claim here by adding together the 30% of Exxon's *total nationwide income* that formula States tax and the 100% of *Alaskan production income* that Alaska taxes. The two are simply apples and oranges.

That 42 formula States collectively levy taxes on 30% of Exxon's nationwide income says nothing about whether Exxon is subjected to actual multiple taxation. In fact, based upon appellants' 1978 to 1980 tax returns in all the States, including Alaska, it is undisputed that during these years Exxon was actually taxed on only 51.4% of its total nationwide income, R. 16923, and therefore benefited from remarkable *undertaxation*. Similarly, ARCO was taxed on only 63.0% of its total income by all the States. *Id.*[22]

B. The *Container Corp.* Decision Controls This Case.

Two years ago, in *Container Corp.*, this Court was confronted with the same erroneous argument made by taxpayers here: that formula apportionment and separate accounting are constitutionally incompatible and necessarily generate double taxation because California's formula taxed a portion of income that was taxed in full by other countries' separate accounting.[23]

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[22] Although Sohio's complicated corporate structure makes a similar straightforward calculation difficult, it appears that Sohio was taxed by all the States on about 95% of its total nationwide income during 1978-80. R. 16925.

[23] *See* Appellant's Brief On The Merits at 9, *Container Corp. v. Franchise Tax Bd.*, No. 81-523 (U.S. July 30, 1982); Brief for Gulf

Applying the "additional scrutiny required by the Foreign Commerce Clause," the Court declined to hold that one division-of-income method is constitutionally preferred. 463 U.S. at 185. Noting that both separate accounting and formula apportionment are "imperfect proxies for an ideal which is not only difficult to achieve in practice, but also difficult to describe in theory," 463 U.S. at 182, the Court concluded, "[W]e have seen no evidence demonstrating that the margin of error (systematic or not) inherent in the three-factor formula is greater than the margin of error (systematic or not) inherent in . . . separate accounting . . . ." *Id.* 183-84.

The Court categorically rejected the contention that the combination of separate accounting and formula apportionment inevitably results in multiple taxation. "Whether the combination of the two methods results in the same income being taxed twice or in some portion not being taxed at all is dependent solely on the facts of the individual case." *Id.* at 188 (footnote omitted). Thus, even though the parties in *Container Corp.* did not dispute that *actual* double taxation had occurred on the particular facts of that case, *id.* at 187 n.22, the Court concluded that "it would be perverse" to hold that the Constitution forbids the use of either method. *Id.* at 193.

C. Taxpayers Misrepresent This Court's Decision In *Exxon v. Wisconsin* And Misapply Cases Dealing With Gross Receipts And Property Taxes.

It is ironic that in attempting to avoid *Container Corp.*, taxpayers rely almost entirely on the decision in *Exxon Corp. v. Wisconsin Department of Revenue*, 447 U.S. 207 (1980). *See* J.S. at i, 10, 11. There, one of these same taxpayers attempted unsuccessfully to persuade this Court that separate accounting for oil production income was constitutionally *required*. Having failed in that attempt, taxpayers here contend that the same method is constitutionally *forbidden*.

Oil Corporation as Amicus Curiae at 5, 17; Brief of Phillips Petroleum Company as Amicus Curiae at 3.

In that case, Exxon argued that because its internal accounting system could separately account for oil production income with accuracy, Wisconsin was constitutionally required to exclude that income from the total income pie against which the State applied its apportionment fraction. In rejecting that contention, the Court reaffirmed a long line of precedents granting wide latitude to the States in their choice of division-of-income methods. 447 U.S. at 219-23; *see Container Corp.*, 463 U.S. at 164.

In upholding Wisconsin's particular application of formula apportionment, the Court recognized that Wisconsin was not attempting to tax a portion of Exxon's production income in Alaska or elsewhere; the Court simply upheld Wisconsin's use of Exxon's nationwide income as the total income pie to which Wisconsin applied an apportionment fraction in order to arrive at an estimate of Wisconsin income. 447 U.S. at 226-27. Thus, the Court did not hold, nor in any way suggest, as taxpayers claim, that "separate accounting may not be used" by some States when other States are constitutionally permitted to use formula apportionment.[24] J.S. at i.

Taxpayers' heavy reliance on property tax cases and gross receipts tax cases[25] is also entirely misplaced. In

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[24] Neither does the holding of *Mobil Oil Corp. v. Comm'r of Taxes*, 445 U.S. 425 (1980), support the taxpayers' argument. In *Mobil*, the exclusion sought by the taxpayer was premised on the legal fiction that dividend income could be taxed only by the State of commercial domicile. Mobil accordingly argued that Vermont was required to exclude from its apportionable base all dividend income from foreign subsidiaries received by the parent company, which was domiciled in New York. The Court's rejection of this attempt to erode the unitary theory on the basis of a legal fiction was predictable, and, as the dissent noted, makes that holding rather "unexceptional." *Id.* at 450 (Stevens, J., dissenting). *Mobil*, then, had nothing to do with separate accounting.

[25] J.S. at 12-14, 19-20 & nn.11-12, citing, *e.g.*, *Japan Line v. County of Los Angeles*, 441 U.S. 434 (1979); *Standard Oil v. Peck*, 342 U.S. 382 (1952); *J.D. Adams Mfg. v. Storen*, 304 U.S. 307 (1938); *Evco v. Jones*, 409 U.S. 91 (1972).

those cases, unlike in net income tax cases, one taxing jurisdiction taxed the whole pie while another taxed a slice, a situation inevitably producing double taxation.

The property tax cases are exemplified by *Japan Line v. County of Los Angeles*, 441 U.S. 434 (1979). In that case, Japan taxed the full value of cargo containers used in international trade, while California taxed a part of the value of those same containers. The result was inevitable double taxation. However, in *Container Corp.*, this Court distinguished the overlapping property taxes found in *Japan Line* from the compatibility of separate accounting and formula apportionment of net income:

> In *Japan Line*, we relied strongly on the fact that one taxing jurisdiction claimed the right to tax a given value in full, and another taxing jurisdiction claimed the right to tax the same entity in part—a combination resulting necessarily in double taxation. . . . Here, by contrast, we are faced with two distinct methods of allocating the income of a multinational enterprise. . . . Whether the combination of the two methods results in the same income being taxed twice or in some portion of income not being taxed at all is dependent solely on the facts of the individual case.

463 U.S. at 188 (citations and footnote omitted).[26]

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[26] Similarly, a gross receipts tax is levied on the total gross proceeds from sale of an article. If a manufacturing State taxes the total gross receipts from out-of-state sales, and a retail-sales State also taxes those total proceeds, multiple taxation is inevitable. This Court has resolved that overlap by permitting the destination State to tax all the gross proceeds, but prohibiting the production or manufacturing States from taxing gross receipts at all. As we have seen, there is no equivalent double taxation when *net* income is divided by separate accounting and by formulas. "The court has almost always been of the opinion that the difference between a tax on gross income and a tax on net income derived from multistate business required a different result when resisted on commerce clause grounds." P. Hartman, *Federal Limitations on State and Local Taxation* § 8:1 (1981).

II. THIS COURT SHOULD DISMISS TAXPAYERS' APPEAL BECAUSE THEY DID NOT EVEN ATTEMPT TO SHOW THAT AS 43.21 DISPROPORTIONATELY ATTRIBUTES INCOME TO THE STATE.

This Court has long recognized that there is a "substantial margin of error inherent in any method of attributing income among the components of a unitary business." *Container Corp.*, 463 U.S. at 184. *See, e.g., Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113, 121 (1920). "[A]rriving at precise territorial allocations of 'value' is often an elusive goal, both in theory and in practice," and it is "[f]or this reason" that this Court "ha[s] long held that the Constitution imposes no single formula on the States." *Container Corp.*, 463 U.S. at 164 (citing *Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 445 (1940)).

Thus, a State's determination that a particular methodology accurately allocates the income of a multistate business must be given considerable deference. *See, e.g., Container Corp.*, 463 U.S. at 176; *Moorman*, 437 U.S. at 274. The Constitution does not invalidate an apportionment method "whenever it *may* result in taxation of some income that did not have its source in the taxing State." *Container Corp.*, 463 U.S. at 169-70 (emphasis in original; quoting *Moorman*, 437 U.S. at 272). Instead, the taxpayer must prove, "by 'clear and cogent evidence' that the income attributed to the State is in fact 'out of all appropriate proportions to the business transacted . . . in that State,' or has 'led to a grossly distorted result.'" *Id.* at 170.[27] Absent such evidence, no substantial constitutional question is presented.

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[27] Quoting *Moorman*, 437 U.S. at 274, quoting in turn *Hans Rees' Sons v. North Carolina ex rel. Maxwell*, 283 U.S. 123, 135 (1931) and *Norfolk & W. Ry. v. Missouri State Tax Comm'n*, 390 U.S. 317, 326 (1968).

A. Taxpayers Have Presented No Evidence Showing That Alaska's Separate Accounting Method Disproportionately Attributes Income To The State.

In the trial court, taxpayers resolutely refused to offer any evidence showing that AS 43.21 attributed to Alaska more oil production income than they in fact earned in the State. The sole "evidence" of disproportionality relied upon by taxpayers here is their calculation of the difference between the taxable income that UDITPA's three-factor formula would have attributed to Alaska, and their taxable income as measured by AS 43.21. Based on this calculation they allege "overtaxation . . . rang[ing] from 279% to 804%." J.S. at 21.

There is absolutely no dispute between the parties that the UDITPA formula would attribute to the State only a fraction of the oil production income measured by separate accounting. Indeed, it was precisely because the Alaska Legislature found that the formula would grossly *underattribute* oil production income to the State, and taxpayers would thus pay only a 2-3% effective tax rate, that it enacted AS 43.21.

As the court below found, the disparity between the results reached by the two income-division methods is caused by marked deficiencies in the accuracy of the three-factor formula when applied to oil production—not by any failing in the separate accounting traditionally favored by major oil-producing States. App. 15a-20a. The Alaska court broke no new ground with that conclusion. All the highest State courts that have considered the question have reached the same conclusion.[28] Alaska has shown (and taxpayers have never disputed) that the

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[28] *See* n.7 *supra*. Those courts found underattribution by the formula comparable to that found here. *E.g.*, *Texas Co. v. Cooper*, 107 So. 2d at 690 (UDITPA income: $1.5 million; separate accounting income: $13 million); *Webb Resources v. McCoy*, 401 P.2d at 890-91 (UDITPA income: $40,000; separate accounting income: $157,000).

formula's assumptions break down when used to attribute oil production income. Taxpayers' inference that UDITPA income is their "actual" Alaska income is, then, no evidence at all.

Taxpayers presented no evidence of what they actually earned in Alaska because they litigated this case as a *per se* attack on separate accounting. As they told the trial court, their theory of the case "requires no elaborate showing that [the tax] is disproportionate to the taxpayer's business within the jurisdiction." R. 12763.

To the contrary, this Court has repeatedly held that a detailed showing of taxpayers' actual in-state income is *exactly* what taxpayers must offer if they are to discharge their burden of showing by "clear and cogent" evidence that a State's method has produced a "grossly distorted result." [29] Indeed, in the only two cases in which this Court has invalidated a State attribution method, the taxpayer used a detailed *separate accounting* analysis to prove overattribution by the formula.[30] Here, however, as in *Moorman*,

> "[The taxpayer] did not attempt to prove the amount of its actual net income from [in-state] activities. . . . *In this era of sophisticated accounting techniques, it should not be impossible for a unitary corporation to prove its actual income from activities in a particular state.* However, [taxpayer] showed only that its tax liability would be substantially less if [the State] employed a three-factor apportionment formula. We have no basis to assume

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[29] *Butler Bros. v. McColgan*, 315 U.S. 501, 509 (1942); *Underwood Typewriter v. Chamberlain*, 254 U.S. 113, 121 (1920); *Norfolk & W. Ry. v. North Carolina ex rel. Maxwell*, 297 U.S. 682, 690 (1936); *Bass, Ratcliff & Gretton, Ltd. v. State Tax Comm'n*, 266 U.S. 271, 283 (1924).

[30] *Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell*, 283 U.S. 123, 134-35 (1931); *Norfolk & W. Ry. v. Missouri State Tax Comm'n*, 390 U.S. 317, 321-22 (1968).

> that the three-factor formula produced a result equivalent to the corporation's actual [in-state] income. . . ."

437 U.S. at 275 n.9 (emphasis added) (quoting with approval *Moorman Manufacturing v. Bair*, 254 N.W. 2d 737, 757 (Iowa 1977) (McCormick, J., concurring)). Thus, taxpayers here simply declined to shoulder the burden of proof placed upon them by this Court's precedents.

B. AS 43.21 Properly Accounts For Out-of-State Contributing Activities.

Instead of proving their actual Alaskan income, taxpayers cite examples of managerial and support activities that take place outside the State. J.S. at 4-6 & n.4, 20 n.22. They then assert that AS 43.21 is invalid because it does not permit a deduction for some unspecified amount of profit allegedly earned by these activities. This argument fails for two reasons.

First, the Constitution simply does not require an income allocation system to account for each and every activity or factor that a taxpayer's choice of economic theories says contributes to net income. In *Moorman*, this Court upheld a single factor sales formula that ignored entirely the contributions to income of both *labor* (the payroll factor) and *capital* (the property factor) outside the State:

> Whatever merit [the assumption that at least some portion of the income from Iowa sales was generated by Illinois activities] might have from the standpoint of economic theory or legislative policy, it cannot support a claim . . . that Iowa in fact taxed profits not attributable to activities within the State . . . . [E]ven were we to assume that the Illinois [manufacturing] activities made some contribution to the profitability of the Iowa sales, appellant's claim that the Constitution invalidates an apportionment formula whenever it may result in taxation of some income that did not have its source in the taxing State is incorrect.

Moorman, 437 U.S. at 272; *accord*, *Underwood Typewriter v. Chamberlain*, 254 U.S. at 120.

Container Corp. confirmed that no income allocation system can take into account all arguable contributions to income. "[E]ven the three-factor formula is necessarily imperfect." 463 U.S. at 182-83 & n.20. Indeed, in the instant case, the three factors ignore entirely the value of the oil, the predominant source of an oil company's production profits. *See* pp. 5-6, *supra*.

Similarly, as the Court said in *Container Corp.*, separate accounting "often ignores or captures inadequately the many subtle and largely unquantifiable transfers of value that take place among the components of a single enterprise." 463 U.S. at 164-65. Indeed, *no* separate accounting law—including those of other oil-producing States and the federal tax code[31]—attributes profit to such activities as research and development, management, and accounting that are ordinarily treated in taxpayers' own books as "cost centers" rather than "profit centers." R. 1527-28.

Here, as in *Moorman*, taxpayers have produced no separate accounting analysis or *any* quantified assessment of the profit, if any, assignable to outside contributing activities under their economic theory.[32] Absent any such

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[31] La. Admin. Code art. 47:244.3.A, B.3 (1975); Miss. Code Ann. § 27-7-23(c)(2)(B) (7 Supp. 1985); Miss. Admin. Reg. 1.27-7-23 (7)(c)(2) (1979); Okla. Stat. Ann. tit. 68, § 2358, A.4.a (West Supp. 1984); *see Magnolia Petroleum Co. v. Oklahoma Tax Comm'n*, 121 P.2d at 1101. *See* Treas. Reg. § 1.482-2(b)(1), (3), (7).

[32] Only one item of "proof" merits discussion. The taxpayers repeatedly assert that the record contains evidence that "80% of the expenses necessary to earn production income from Alaskan oil were incurred *outside* Alaska." J.S. at 4-5, 20-21 n.22 (emphasis in original). This assertion is based solely on one conclusory paragraph in an affidavit submitted by the taxpayers. App. 285a. Their affiant, however, confused the cost of *producing* Alaskan oil with the post-production cost of *transporting* the oil to refineries. Of the $380 million he assigned out of the State (his "80%"), fully $350 million were tanker charges incurred in transporting the oil from Alaska to refineries.

showing, taxpayers' anecdotes cannot raise a substantial question as to the constitutionality of AS 43.21.

Second, despite their protests to the contrary, taxpayers *can* deduct such outside profits as they report to their own shareholders.[33] 15 AAC 21.290(b). In allowing such a deduction, AS 43.21 goes beyond traditional separate accounting and far beyond what *Moorman* and *Container Corp.* require—in taxpayer's favor. Taxpayers claim, however, that SEC regulations forbid them to allocate oil production profits to out-of-state support activities in their shareholder reports because it would be "misleading or inaccurate" to do so. J.S. at 17 n.18. In essence, then, taxpayers assert that the Constitution requires Alaska to permit an attribution of profits to outside support activities that taxpayers themselves contend is "misleading or inaccurate." That is absurd.

In sum, taxpayers did not attempt an actual accounting of just how much they *did* earn in Alaska. Because they failed even to try to make the required showing of gross overattribution of income, their appeal does not raise a substantial federal question.

III. NONE OF TAXPAYERS' OTHER POINTS IS SUBSTANTIAL.

A. Alaska's Corporate Income Tax Statute Is Internally Consistent.

Every State's income tax law must have "internal consistency"—that is, "if [the State's law were] applied by every jurisdiction, it would result in no more than all of the unitary business' income being taxed." *Container Corp.*, 463 U.S. at 169.

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[33] On this matter of state law, the decision of the Alaska Supreme Court is conclusive and unreviewable. Taxpayers

> may amend their tax reports and returns to deduct any outside-generated profits attributable to general overhead and administrative activities associated with Alaskan oil production not previously deducted.

App. 12a.

AS 43.21 met this test. It divided a taxpayer's income into two categories. First, oil production income was determined by separate accounting. Obviously, if every State used the same separate accounting method for oil production income, each taxpayer would be taxed on exactly 100% of its nationwide production income.

Second, Alaskan income from other activities was estimated by an apportionment formula in which (1) *worldwide* oil production income was *excluded* from the apportionable base; (2) all sales, property and payroll associated with oil production in Alaska were *excluded* from the in-state factors in the formula (*i.e.*, the numerators); and (3) all sales, property and payroll associated with oil production *outside* Alaska were *included* in the *worldwide* factors contained in the formula's denominators. AS 43.21.040. The effect of the formula used by Alaska to estimate taxypayers' non-production income was thus to slightly underestimate non-production income. If all States used this system, it is mathematically inevitable that *less* than 100% of a corporation's non-production income would be subject to tax. Consequently, AS 43.21 more than satisfied the "internal consistency" test.[34]

B. Alaska's Division-of-Income Method Does Not Discriminate Against Interstate Commerce.

Alaska's 9.4% corporate income tax applies uniformly to the Alaskan income of every corporation doing business in the State, regardless of where the company is headquartered, or whether it is a domestic or an interstate business. Thus, in contrast to the laws at issue in the cases relied on by taxpayers,[35] Alaska has treated in-

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[34] Incomprehensibly, taxpayers' argument to the contrary—and the affidavits cited in support of it—explicitly assume that other States would *not* apply exactly the same rules as Alaska's. J.S. at 25-26 & n.29. The internal consistency test articulated by this Court, however, is designed to determine what happens when the taxing State's rules *are* identically applied by all States.

[35] *Metropolitan Life Ins. Co. v. Ward*, 105 S. Ct. 1676 (1985) (statute imposed lower gross premiums tax rate on domestic insur-

state and out-of-state taxpayers in an identical fashion.[36]

In *Container Corp.* this Court recognized that if a facially-neutral tax law like AS 43.21 fairly apportions income, that is, does not produce a "grossly distorted result," 463 U.S. at 169-70, the law does not violate the Commerce Clause's anti-discrimination principle.

> Aside from forbidding the obvious types of discrimination against interstate or foreign commerce, [the anti-discrimination] principle might have been construed to require that a state apportionment formula not differ so substantially from methods of allocation used by other jurisdictions in which the taxpayer is subject to taxation so as to produce double taxation of the same income, and a resultant tax burden higher than the taxpayer would incur if its business were limited to any one jurisdiction. At least in the interstate commerce context, however, the anti-discrimination principle has not in practice required much in addition to the requirement of fair apportionment.

Id. at 170-71. The Court thus reaffirmed the conclusion it had earlier reached in *Moorman*—that to eliminate "all overlapping taxation would require this Court to establish not only a single constitutionally mandated method of taxation, but also rules regarding the application of that method in particular cases." *Id.* at 171 (citing *Moorman*, 437 U.S. at 278-80). Because that

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ance companies); *Armco, Inc. v. Hardesty*, 104 S. Ct. 2620 (1984) (wholesale gross receipts tax exempted local manufacturers); *Westinghouse Elec. Corp. v. Tully*, 104 S. Ct. 1856, 1860 (1984) (tax credit limited to products shipped from the State); *Boston Stock Exch. v. State Tax Comm'n*, 429 U.S. 318 (1977) (transfer tax taxed out-of-state securities transactions more heavily).

[36] Taxpayers make the baseless allegation that enactment of AS 43.21 "allowed Alaska to . . . reduce the tax rates on local businesses." J.S. at 3. This grave charge is absolutely false: Alaska does *not* impose different tax rates on local businesses. There is no basis in fact for taxpayers' allegations, and the part of the record cited by taxpayers does not offer even the slightest support for their charge.

function is constitutionally reserved to Congress, the Court expressly declined to undertake it. *Id.*

Taxpayers assert that the Commerce Clause forbids a State to "tailor" a tax by using a different division-of-income method for one industry than it uses for other industries. But as set forth above, UDITPA expressly contemplates that States will modify their prevailing division-of-income method where that method does not "fairly represent the extent of [a] taxpayer's activity in [the] State." *See* pp. 5-6, *supra*. The vast majority of States *do* use special division-of-income methods, including separate accounting, to determine the in-state income of businesses in a broad variety of industries. *See* Appendix, listing a sampling of more than sixty industry-specific division-of-income rules used by the States.

The necessary result of the argument proposed by taxpayers would be to require every State to use a single division-of-income system for all industries, and thus hold unconstitutional *all* of these provisions. That result is flatly inconsistent with this Court's refusal in *Container Corp.* and *Moorman* to mandate uniform division-of-income rules, out of deference to the proper role of the States, and to Congress. *See Container Corp.*, 463 U.S. at 171; *Moorman*, 437 U.S. at 278.

C. The Measure Of Alaska's Income Tax Is Reasonably Related To Taxpayers' Alaskan Activities.

In *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 628-29 (1981), this Court held that Montana's coal severance tax satisfied the Commerce Clause because the measure, or incidence, of the tax was reasonably related to the taxpayer's coal-mining activities, or presence, in the State as measured by the number of tons of coal produced.[37] Thus, because Alaska's tax is reasonably re-

[37] Both the majority and the dissenters in *Commonwealth Edison* agreed that a general revenue measure—such as a corporate income tax—necessarily satisfies this requirement. *See* 453 U.S. at 622 (majority opinion) and *id.* at 651 (Blackmun, J., dissenting).

lated to appellants' oil production activities in the State, as measured by the amount and value of oil produced, it fully satisfies the *Commonwealth Edison* standard.

Taxpayers' argument to the contrary rests on the assertion that Alaska's use of separate accounting is unconstitutional because a taxpayer's Alaskan oil production income may remain the same regardless of whether certain support services take place in or out of the State. But as stated above, the *Moorman* decision explicitly recognized that a division-of-income method need not take into account all factors that may contribute to the earning of income, so long as the method does not lead to a grossly distorted result.[38] 437 U.S. at 273. Because Alaska's separate accounting reasonably estimates taxpayers' Alaskan income, the measure of Alaska's tax is reasonably related to in-state activities.[39]

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[38] Indeed, the one-factor sales apportionment formula upheld in *Moorman* necessarily attributed the same income to Iowa regardless of whether all or none of the taxpayer's payroll and property were located in the State.

[39] There is no truth whatsoever to taxpayers' intimation that by using separate accounting, Alaska is taking anything from other States, or imposing a tax on a national resource that will somehow be exported to consumers in other States. No other formula apportionment State's tax calculation is affected by whether Alaska uses separate accounting or a formula. And since the price of crude oil is determined by the world market, taxpayers cannot and do not "export" the income tax they pay to out-of-state consumers. If this Court were to hold that Alaska was constitutionally required to use formula apportionment for oil production income, the only results would be an additional windfall of $2 billion to these three oil companies, and a devastating blow to the State.

Finally, taxpayers' claim that "[w]hen it enacted the Oil Tax, Alaska projected that in 20 years its oil taxes would result in" an alleged "transfer of wealth from the Lower 48 to Alaska equal to $1,000 for every American," J.S. at 3 n.1, is also completely false. The budget projection to which taxpayers refer was made in 1981, when AS 43.21 was *repealed*, *not* when it was enacted. The projection was for increases in Alaska's Permanent Fund, which derives from *royalty* receipts, and interest on those receipts, *not*

IV. PRUDENTIAL CONSIDERATIONS OFFER ADDITIONAL REASONS FOR NOT GIVING PLENARY REVIEW TO THIS APPEAL.

In addition to the insubstantiality of the questions presented, significant prudential factors—the unbroken line of court decisions upholding the constitutionality of separate accounting; the constitutional allocation of primary responsibility for regulating interstate commerce to Congress; the broad discretion afforded States in matters of taxation; and the pendency of presidential and congressional initiatives to limit the use of worldwide formula apportionment—counsel against giving plenary consideration to this appeal.

Separate accounting has long been the prevailing method oil-producing States have used to determine in-state oil production income. Yet *every* court that has considered the constitutionality of using separate accounting to determine oil production income has upheld its use.[40] Indeed, as the Supreme Courts of Kansas and Oklahoma both found, "[W]here the direct method of income allocation [separate accounting] can be employed, all suspicion of unconstitutional taxation is dispelled." *Webb Resources v. McCoy*, 401 P.2d at 889; *Magnolia Petroleum v. Oklahoma Tax Commission*, 121 P.2d at 1011. In light of the lower courts' unanimity on the question presented by this appeal, plenary review is unnecessary.

In *Moorman*, this Court recognized that the development of uniform rules for dividing the income of multistate businesses "would require a policy decision based on

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from corporate income or other tax revenues. AS 37.13.010(a). At that time, oil prices were expected to continue to rise. Royalties are due the State because the oil is produced from State land. None of this relates to income taxes, and in any event, not a penny of "wealth" would have been "transferred" from the lower 48.

[40] *See Texas Co. v. Cooper*, 107 So. 2d at 688; *Magnolia Petroleum v. Oklahoma Tax Comm'n*, 121 P.2d at 1011-12; *Webb Resources v. McCoy*, 401 P.2d at 889-91.

political and economic considerations that vary from State to State. . . . *It is to [Congress], and not this Court, that the Constitution has committed such policy decisions.*" 437 U.S. at 279-80 (emphasis added). "Congress has long debated, but has not enacted, legislation designed to regulate state taxation of income." *Container Corp.*, 463 U.S. at 196-97 (quoting *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 448 (1980)).

This Court has repeatedly recognized that in the absence of congressional action, the States must be given broad discretion in matters of taxation.[41] In their appeal, taxpayers would have this Court drastically constrict the States' traditionally broad taxing power by imposing a uniform division-of-income method, even though Congress has refused to do so. In the face of Congress' persistent refusal to require States to use formula apportionment, this Court should not give plenary consideration to an appeal requesting such a result.

While Congress has not adopted legislation requiring the States to use uniform division-of-income methods, recent developments suggest that some limitations on the use of worldwide formula apportionment may soon be enacted. On November 8, 1985, the President announced his support for prohibiting the States from applying formula apportionment to the worldwide income of a taxpayer who operates both in a State and abroad, thereby requiring the use of separate accounting to divide a taxpayer's foreign income from its U.S. income. In so doing, he instructed "the Secretary of the Treasury to initiate the process of crafting Federal legislation to incorporate these principles into law and to work with the Congress for passage."[42] Congress currently has pending before it

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[41] *See, e.g., Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 445 (1940); *Norfolk & W. Ry. v. Missouri State Tax Comm'n*, 390 U.S. 317, 326 (1968).

[42] Statement by the President, State Taxation of Multinational Corps., 21 Weekly Comp. Pres. Doc. 1368 (Nov. 8, 1985).

legislation introduced earlier this year that would essentially adopt those principles. S. 1113, 99th Cong., 1st Sess. (1985).

Plenary consideration of taxpayers' wholesale attack on separate accounting would be particularly unfortunate at this time because it would cast a cloud of constitutional uncertainty over the current climate of active presidential and congressional initiatives to restrict the use of formula apportionment.

CONCLUSION

For the reasons stated above, this Court should dismiss this appeal or summarily affirm the judgment below.

Respectfully submitted,

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APPENDIX

Examples of State Statutes and Regulations Embodying Division-of-Income Rules Different From UDITPA Formula Apportionment

Construction: Miss. Admin. Reg. 1.27-7-23(7)(m) (1979) (separate accounting); [Oregon] St. & Loc. Tax Serv. (P-H) ¶ 65,325.10 (Aug. 11, 1943), ¶ 65,330.20 (Dec. 14, 1955) (separate accounting); Va. Code § 58.1-419 (1984).

Mining and Natural Resource Production: La. Admin. Code art. 47:244.3.B(1975) (separate accounting); 1985 Minn. Sess. Law Serv. art. 1 § 45 (West) (amending Minn. Stat. Ann. § 290.19 (West Supp. 1985)); Miss. Admin. Reg. 1.27-7-23(7)(o) (1979) (separate accounting); Okla. Stat. Ann. tit. 68, § 2358, A.4.a (West Supp. 1984) (separate accounting).

Realty Management: [Oregon] St. & Loc. Tax Serv. (P-H) ¶ 65,330.30 (Nov. 1, 1960) (separate accounting).

Financial Organizations: Ill. Ann. Stat. ch. 120, § 3-304 (c) (Smith-Hurd Supp. 1985); 1985 Ky. Rev. Stat. & R. Serv. § 141.120(10) (Baldwin); La. Rev. Stat. Ann. § 47:245(E) (West 1970); Mich. Stat. Ann. § 7.558(65) (Callaghan 1984); N.D. Corp. Income Tax Return, [1985] St. Corp. Income Tax Forms (CCH), at 17,102 (1984); Or. Admin. R. 150-314.280-(E) (1977); Va. Code § 58.1-418 (1984); Wis. Admin. Code § [Dept. of Rev.] 2.49 (1973).

Insurance: Conn. Gen. Stat. Ann. § 12-218a (West 1983); Fla. Stat. Ann. § 214.72(1)(a) (West Supp. 1985); Ill. Ann. Stat. ch. 120, § 3-304(b) (Smith-Hurd Supp. 1985); Mich. Stat. Ann. § 7.558(62) (Callaghan 1984); Or. Admin. R. 150-314.280-(E) (1977).

Public Utilities: 1985 Ky. Rev. Stat. & R. Serv. 141.-120 (10) (Baldwin); Miss. Admin. Reg. 1.27-7-23(7)(l) (1979); Mo. Ann. Stat. § 143.451(6) (Vernon 1976);

N.C. Gen. Stat. §§ 105.130.4(n),(q),(r) (1979); N.D. Cent. Code § 57-38-13(8) (1983); Or. Admin. R. 150-314-280-(E) (1977); S.C. Code Ann. § 12-7-640 (Law. Co-op. Supp. 1985); Wis. Admin. Code § [Dep't of Rev.] 2.50 (1973).

Transportation (general): Fla. Stat. Ann. § 214.72(2) (West Supp. 1985); Ill. Ann. Stat. ch. 120, § 3-304(d)(1) (Smith-Hurd Supp. 1985); La. Rev. Stat. Ann. § 47:245 (C) (West 1970); Mich. Stat. Ann. § 7.558(57) (Callaghan 1984); Or. Admin. R. 150-314.280-(G) (1983); Pa. Cons. Stat. Ann. § 7401(3)(2)(b) (Purdon Supp. 1985).

Air Carriers: Cal. Rev. & Tax Code § 25101.3 (West 1979); Conn. Gen. Stat. Ann. § 12-244 (West 1983); La. Rev. Stat. Ann. § 47:245(A) (West 1970); Miss. Admin. Reg. 1.27-7-23(7)(j) (1979); Wis. Admin. Code § [Dep't of Rev.] 2.46 (1973).

Motor Carriers: Conn. Gen. Stat. Ann. § 12-218(c) (West 1983); Kan. Stat. Ann. § 79-3279 (1984); Miss. Admin. Reg. 1.27-7-23(7)(k) (1979); N.C. Gen. Stat. § 105-130.4(o) (1979); Va. Code § 58.1-417 (1984); Wis. Admin. Code § [Dep't of Rev.] 2.47 (1973).

Pipelines: Ill. Ann. Stat. ch. 120, § 3-304(d)(2) (Smith-Hurd Supp. 1985); La. Rev. Stat. Ann. § 47:245 (B) (West 1970); Mich. Stat. Ann. § 7.558(58) (Callaghan 1984); Miss. Admin. Reg. 1.27-7-23(7)(i) (1979); Pa. Cons. Stat. Ann. § 7401(3)(2)(c) (Purdon Supp. 1985); Wis. Admin. Code § [Dep't of Rev.] 2.48 (1973).

Railroads: Kan. Stat. Ann. § 79-3279 (1984); Miss. Admin. Reg. 1.27-7-23 (7)(l) (1979); Mo. Ann. Stat. § 143.451(4) (Vernon 1976); N.C. Gen. Stat. § 105-130.4(m) (1979); Va. Code § 58.1-420 (1984).

Water Transportation: Or. Admin. R. 150-314.280-(H) (1984), (J) (1973).

Passenger Carriers: Mo. Ann. Stat. § 143.451(3) (Vernon 1976); N.C. Gen. Stat. § 105-130.4(p) (1979).

Service Enterprises: La. Rev. Stat. Ann. § 47:245(D) (West 1970).